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THE NATIONAL CITY BANK OF NEW YORK

1934

Economic Conditions Governmental Finance United States Securities

New York, May, 1934.

General Business Conditions

THE changes in the business situation during April have presented more of mixed aspect than in the earlier months of the year, due to divergent movements in the industries and in the markets for farm products. In the industries both operations and employment have made fresh gains. Curtailment has appeared in coal mining and in some of the lighter industries which evidently have passed their Spring peak, but it has been offset by pronounced increases in automobile and steel production. Of course the importance of these two industries in general business is so great that any month in which they are expanding is certain to be a period of improvement in many other lines.

Many of the automobile manufacturers, especially the makers of the three leading low-priced cars, have driven their plants during April to their practical capacity. They are experiencing a good sales demand, their dealers were poorly stocked for the Spring season, and as they are by no means sure of escaping further labor troubles they have been anxious to get all the cars possible into dealers' hands. Hence the only limit on their output has been the ability to produce, and the estimated outturn of about 400,000 cars and trucks is the highest in any month in four years.

The steel mills have a heavy backlog of unfilled orders, received after they had given notice of price advances at the beginning of the month. Operations in the last week of April were at 54 per cent of capacity, according to the Iron and Steel Institute. This is the highest since last August, and compares with a peak of 59 per cent last July. Trade authorities agree that if all the tonnage contracted for is to be delivered before July 1, as the code requires, mill operations must make a further advance. To be sure, part of the spurt may be at the expense of Summer operations, due to requirements having been covered beyond the second quarter. However, the present situation is a strong one.

Some of the laggard industries such as the manufacturers of electrical and railway equipment have better sales and larger unfilled orders, indicating that the obsolescence and wearing out of equipment, and the improved will to buy, may be turning the tide in that quarter as well as in the automobile situation. Taken as a whole, industrial operations have increased by more than the usual seasonal percentage, according to the preliminary figures. This is the fifth successive month of improvement, and such a showing, with all that it signifies in the way of increased employment and satisfactory consumer demand, naturally generates optimism.

Farm Price Weakness

On the other hand, the reappearance of weakness in prices of the chief farm products, including the grains, cotton and hogs, is a counterbalance to the good industrial reports. It is the more disturbing because it comes at a time when the prices of the goods offered for sale to the farmers are mounting rapidly. Within the month further wage increases and price advances have been put into effect not only in steel, but in coal, automobiles, and other industries. Steel and coal are basic materials, whose higher prices will have multiplied effects upon costs and prices of finished products of all kinds. Eventually all these increases will have to be paid by farmers and other consumers.

The aim of all the efforts that have been made on behalf of agriculture, and indeed of the general policy of advancing commodity prices, has been not only to raise the actual prices of agricultural products, but to advance them relative to other prices, so that the farmer can buy more of other goods with his produce. But the trend in the past month has been against the farmer on both sides of the account, and hence toward restriction of his buying power.

Moreover, the price declines in products wherein tremendous efforts have been made

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by the A. A. A. to adjust the supply to the demand carry the implication that these efforts are ineffective. They tend to keep alive fears that further attempts to raise prices by monetary measures will be demanded, or at best that Government bounties to agriculture and high processing taxes upon farm products will be indefinitely continued. It is in order to point out that the declines themselves are evidence of the inability of monetary influences to uphold prices when the factors of supply and demand in each market take an unfavorable turn.

The Decline in Grains

The wheat situation is generally accounted the most important agricultural situation in this country, though this is probably less true than formerly. The dominant facts in the wheat situation are that the United States price is too high to compete with other countries in the export markets, and that the supply is too large for our people to consume by themselves. The Chicago market has been around 20 cents above Liverpool and 18 above Winnipeg, whereas on an export basis it would be lower than either. A statement by the Department of Agriculture on wheat prospects suggests that the carryover at the end of the present crop year will be around 275,000,000 bushels, and the Winter wheat crop is officially estimated at 492,000,000, with the possibility that it may be larger, in view of favorable reports since the estimate. If Spring wheat yields should be average and the acreage should be as indicated by the report on intentions to plant, the yield would be 240,000,000. However, the Spring wheat states are very dry, and this may affect the crop.

Altogether these figures suggest a possible supply of 1,000,000,000 bushels, whereas the Department's allowance for probable domestic use is 625,000,000, including 500,000,000 for food, 75,000,000 for seed, and 50,000,000 as feed. Such an outcome would erase the improvement in the statistical position that occurred as a result of the short crop last year.

Secretary Wallace has discussed this prospect in press conferences with his usual frankness, having made statements to the effect that a nation which produces more wheat than it consumes cannot be expected to hold its prices indefinitely above the world price, and that the disparity might be corrected by a decline here as well as an advance abroad. This is a sufficient explanation of the drop of about 12 cents during the month; but as this leaves Chicago still 12 cents above Liverpool, evidently the prospect for recovery is not very heartening unless there is a crop setback, or unless further Government supporting measures are employed.

Corn and oats likewise have had a sharp drop. The small crops of these feed grains last season, followed by the Government's attempt to support corn by lending 45 cents a bushel on farm stocks, have held prices too high in relation to cattle, hogs, butter, eggs and poultry; hence the amount fed has been reduced. Moreover, there have been fewer animals to feed. The Corn Belt states had 8.5 per cent fewer cattle on feed and 8 per cent fewer hogs on farms on January 1, compared with a year ago, and since then the slaughter has been heavier, due to the inability to make a profit out of feeding operations. Record stocks of corn have accumulated at the terminals, and have had a weakening influence on the market.

Farmers' planting intentions indicate a reduction of about 10 per cent in the corn acreage, which is the chief hope of recovery unless there is a substantial improvement in hogs, dairy and poultry prices. Even so the 260,000,000 bushels now locked in farmers' cribs will remain to be disposed of. The apprehensions as to the disposition of this stock illustrate the disturbing aftermath of attempts to peg prices, and the complications that come from interference in the markets. In fact, the whole disturbance in the feed grain situation is partly a consequence of the effort to improve hog prices by the pig slaughter carried out last Fall; and the expected reduction of farrowings under the present hog-corn plan will have additional complications for the grain producers if they have a favorable growing season.

The most favorable development from the Western States is the rise in cattle prices, accompanying smaller receipts since the end of March. Hog prices, on the other hand, have declined.

Bankhead Bill Signed

Cotton has shared the decline of the grains, with a break of nearly 2 cents from the top, and the cotton situation is one of great interest. The Bankhead bill to restrict the crop to 10,000,000 bales, which we discussed at some length last month, has become law, but the conference restored the House provisions fixing the tax on any cotton produced in excess of the allotments at 50 per cent of the price instead of 75 per cent, and making the tax payable when the cotton is sold instead of when it is ginned. Evidently it is the view of the market that these provisions will be ineffective as a deterrent to production. The farmer will be able to hold any excess cotton in his barn without much cost; and indeed if he wishes to sell it and pay the tax he will receive substantially more than the cost of picking it, while the ginning cost can be covered by the seed. Hence he stands to gain by

picking all he can grow. If he has a smaller acreage to cultivate he will be able to give it better cultivation and with a prospect of a higher price may take a chance on expending more for fertilizer.

If the farmer reasons in this way the bill is not likely to have much effect. Probably no one will be greatly disappointed except its sponsors. If the plan worked as intended, its cumulative economic effects would be unfavorable, raising the cost of production and providing a new incentive for the substitution of other fibers for cotton and the stimulation of foreign growths. As it is, the course of the market will as usual depend principally upon the crop reports during the growing season, and the general economic situation. Meanwhile Secretary Wallace has the task, described by himself as "abhorrent", of enforcing the bill, devising the quotas, and providing for the tagging of all the cotton now in existence, which is tax exempt.

Effects of Price Increases

Unquestionably the events of the month have added to Secretary Wallace's difficulties in more than one way, and through the developments outside of agriculture as well as those within it. All advances in industrial costs and prices are at the expense of the farmer, whose purchasing power is not a wage scale, but the return from his products in the open market. He is supposed to be compensated for higher prices for goods bought by higher prices for goods sold, provided by the A. A. A.; but of course the rising prices of the things he buys place the A. A. A. in the position of aiming at goals which are constantly moving higher, and thus the disparity is kept alive.

The purpose of the Farm Act is to restore to the farmer the "fair exchange value", which is defined as the 1909-14 average purchasing power of farm products with respect to articles farmers buy. According to the calculations of the Department of Agriculture these values at the time of the passage of the Act were, in terms of prices on the farm, 88.4 cents for wheat, 12.4 for cotton, 7.24 for hogs, and 64.2 for corn. Since the Act was passed the prices of goods purchased have advanced by about 20 per cent, and a recalculation of the foregoing farm prices would therefore place them approximately at $1.06 for wheat, 15 cents for cotton, 8.70 for hogs, and 77 cents for corn.

A comparison of these with current prices measures the added difficulties that the industrial cost increases have already made for the farm program. Their effects are mitigated by the distribution of artificial purchasing power to the farmer in the form of Government bounties, but improvement due to this cause can only cover up the disparity and can last no longer than the bounties last.

Wage Increases in the Industries

The automobile industry, which has given the "Spring rise" its principal support, is one of those which is concerned with the farm situation. Following an advance at the end of March of 11 per cent in hourly wage rates and a reduction in working hours from 40 to 36 a week, the members of the National Automobile Chamber of Commerce have raised prices $25 a car and up. It is too early to judge the ultimate effects of the advance upon sales, and doubtless they will depend upon the later course of farm prices, developments in the capital goods industries, and other general factors. If automobiles were bought only by workers in the automobile factories and in the other industries where money wages have been raised the price increase would merely be an offset to the higher wage. But to the farmer it is one of the factors tending to nullify the Government's effort to restore his price parity. Also, there are other groups of the population, in the aggregate a very important part of the automobile market, who have had no increase of income from the N. R. A. policies. The price advance diminishes their ability to buy. There are still other workers, 8,000,000 or more in number, largely in the capital goods and service industries, who have little employment or none at all and are living upon slender resources or governmental assistance, and what is the probability of their getting work if higher prices tend to reduce the markets for manufactured goods?

The above does not imply that the new automobile prices are without reason. The hourly wage rate in the industry is now established equal to or above the highest paid in 1929, and the prices of its materials have been rapidly advanced by similar wage policies in other industries. Everyone admits that automobile prices, now as before, give values for the money unexcelled by any industry. However, the sale of the product will not depend on the justification for the advance, but upon the purchasing power of the consumer.

Nor would the increase be a matter of concern if only the automobile industry were raising prices. But the rise in costs all along the line is causing advances in the prices of a great variety of finished products and services. The press gives citations too numerous to mention, ranging from hotel charges to books and bread. Moreover, the advances caused by the codes are likely to go further as inventories of lower-priced materials and finished goods made at lower costs are ex-

hausted. The farm implement industry is now at that point, and the tire industry, which has been operating on stocks of low-priced rubber, is approaching it. It has been estimated that some tires today are selling as much as 25 per cent below replacement costs.

1929 Rates Restored

According to a statement by the American Iron and Steel Institute the new wage scale in that industry is 6 to 7 per cent higher than the 1929 peak, and the new prices are about 5 per cent below the 1929 level. The new bituminous coal wage scale, giving the miners a 7-hour day and 5-day week instead of the 8-hour day and 5-day week established by the code last Fall, represents an increase of around 25 per cent in the hourly wage rate. Prices are the highest ever recorded except under wartime or strike conditions causing a scarcity of coal, which of course does not now exist. By contrast, the farmer is receiving prices lower even than in 1913.

The building industry is another in which costs have been rising rapidly, due to the effects of the codes on both construction wages and prices of materials. A compilation by the Dow Service reports of New York shows that a residence which cost $5,000 before the depression could have been built for $2,560 one year ago, but the cost is now back to $4,675, due to "the bulk effect of the codes." This is not a heartening outlook for residential construction, despite the Government surveys which show that this is the one class of building that is really needed. During the first three weeks of April contracts for residential building were 17.4 per cent less than in March, taking the daily average, but 12.4 over last year. The public works classification also declined from March, by 9.6 per cent, but was nearly five times the 1933 figure. Total awards were off 15.9 per cent on the month, and up 146.2 on the year.

The hopeful factor in the building situation is that public works expenditures will increase hereafter, not reaching the peak until mid-Summer. Out of $462,000,000 of contracts awarded in the Eastern states in the first quarter, $350,000,000 were publicly financed.

Attitude of Employers

The reasons for the wage increases by the industries should be plainly understood. They have been established in support of a public policy to that end and also as a move to avert strikes and wasteful disputes over the question of what organizations should represent labor in collective bargaining under the National Recovery Act. With no claims or complaints pending as to wages or conditions of labor, strikes were being worked up upon the issue of what methods of settlement should govern if and when controversy arose in the future. The strike threats were a menace to the recovery; and in the view of the automobile and steel manufacturers, as stated in the hearings on the Wagner bill during the month, the placing of all of labor's bargaining power in the hands of national unions would likewise be a menace. Each manufacturer envisages the hazard of a walkout due to disputes not in his own plant, but elsewhere; and each is concerned over the possibility of such concentration of authority over labor as might lead to general strikes throughout one industry or even in all industries. These views run through the testimony on the Wagner bill, and the wage increases were accepted by the industries as necessary strategy under the circumstances, and as demonstrating that their stand on the larger question involved no lack of cooperation with the public policy.

However, the reasons for the increases do not alter the fact that they constitute a hardship upon the public, through the price advances made necessary, and that they tend to cause further inequalities in relationships within the economic system.

It is erroneous to conceive that these wage increases will more truly serve the interest of labor than of the farmer or other consumers who do not share them. Such a view would imply a conflict of interest, whereas in truth the prosperity of all members of the economic organization requires fair price relations among them, so that the products of each may be exchanged for the others on sound terms, leading to full and free trade. The error is in viewing money as the source of purchasing power, or in considering that there is any other source than in the exchange of goods and services. To the extent that money wage increases lead to price advances and rises in the cost of living their value to labor is lost, and if they lead in addition to reductions in sales, declines in production, and decreases in employment they make the situation worse than it otherwise would be. The whole depression has been a prolonged demonstration of that fact.

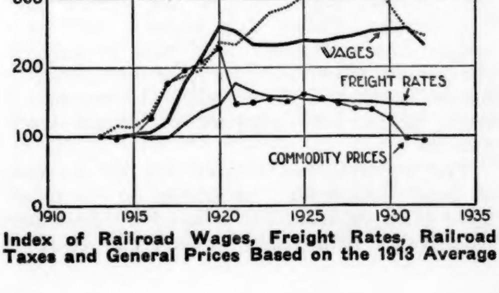
Railway Wage Increase

The agreement between railway company officials and the officials of the employe brotherhoods to restore the 10 per cent wage reduction which went into effect on February 1, 1932, obviously diminishes the probability of any general downward revision of freight charges in the near future, as an aid to business recovery. Rail wages were raised during the war and years following as a necessary accompaniment of rising living costs, which at the peak in 1920 were calculated by the Bureau of Labor Statistics to be about 116% above the 1913 level. The adoption of the eight-hour

day in response to the demands of the employes caused a further increase in hourly wages in order that aggregate weekly and monthly wages might remain the same as under the ten-hour day, with the result that increases in hourly wages after 1913 amounted, on the average for all classes of railroad employes, to more than 150%. The railroads met this increase in their operating costs to a great extent by improvements in operating methods and equipment, but the new equipment involved extensive additional investments of capital, which of course had the effect of partially cancelling the gains by increasing the annual capital charges. However, by reason of the economies thus accomplished railway charges upon traffic were not increased in proportion to the increase of rail wage rates.

Meantime, after 1929, the general level of commodity prices and living costs, which had been the basis of all the wage increases after 1913, was declining rapidly. When the 10% reduction in railway wages went into effect on February 1, 1932, the cost of living already had been reduced much more than that. It was 116% above the 1913 level in 1920, but only 71% above in 1929, 46% above in December, 1931, 36% above in June, 1932, and in June, 1933, had fallen to only 28% above the 1913 level. Thus the basis for the increase of 150% in railroad wages had largely disappeared. By reason of this decline in living costs the railroad employes even in 1929 were enjoying a very large increase in real wages over both 1913 and 1920, and from 1929 to 1932 the wages of those who had employment were steadily increasing in purchasing power, which illustrates the meaning of the term "real wages." Despite the reduction of money wages in 1932, real wages were higher in 1932 than in 1931, and higher in 1933 than in 1932. In short, rail workers who were fortunate enough to have full time employment were enjoying a constant increase of real wages from 1929 down to a few months ago, when for reasons described above living costs began to rise against them.

We reproduce below a chart which appeared in the October, 1932 number of this publication, showing the relations between commodity prices, railroad wages and taxes and freight rates from 1913 to 1932 and also from the same issue a table giving a list of twelve important agricultural products and showing the freight charges thereon per 100 lbs. between Chicago and New York in 1913 and 1932, together with wholesale market quotations on these products in both years:



Index of Railroad Wages, Freight Rates, Railroad Taxes and General Prices Based on the 1913 Average

Freight Rates on Farm Products, Carload Lots, Chicago to New York and Comparative Prices in Chicago Wholesale Markets, 1913-1932

Commodity and Measure	Wholesale Prices Year 1913	Wholesale Prices July, 1932	Per Cent Change	Freight Rates Per 100 Pounds 1913	Freight Rates Per 100 Pounds 1932	Per Cent Change
Cattle .... cwt.	$8.507	$8.606	+1.2	$.28	$.53	+ 89
Hogs .... cwt.	8.365	4.856	—42	.30	.61	+103
Sheep .... cwt.	7.794	5.906	—24	.30	.665	+122
Wheat .... bu.	.986	.484	—51	.212	.38	+ 79
Corn .... bu.	.625	.319	—49	.212	.38	+ 79
Eggs .... doz.	.226	.133	—41	.65	.965	+ 48
Dressed Poultry.... lb.	.145	.156	+ 8	.50	.965	+ 93
Cheese .... lb.	.142	.112	—21	.50	.78	+ 56
Butter .... lb.	.310	.173	—44	.75	.965	+ 29
Meats (Beef)........ lb.	.130	.142	+ 9	.45	.81	+ 80
Milk (a) .... cwt.	1.590	1.060	—33	.372	.529	+ 42
Cotton (b) .... lb.	.128	.058	—55	.575	.86	+ 50

(a) Price paid to farmers in upstate New York; freight rates to New York from 201-210 mile zone. (b) Price in New York for middling, upland; freight rates from Memphis, Tenn., to Fall River, Mass.

Note: Since the above table was printed the plus signs before the cattle, beef and poultry prices of 1932 have been eliminated. None of the commodities named is now above the 1913 level and average of all the prices is below the average of 1932.

It should be said in this connection that owing to the general rise of wages throughout the industries the total of railway operating costs increased nearly in correspondence with railway wage costs. That the companies could not meet these costs without an increase of income is evident from the fact that in 1932 companies having 75 per cent of the total mileage were unable to meet their fixed charges from earnings, although many of them were able to do so with the aid of borrowed money, largely supplied by the Reconstruction Finance Corporation. This cannot be regarded as a permanent solution of the railway problem.

The chart and table show the higher railroad operating costs and charges, together with falling prices for agricultural products.

Even now when the pledge is given to restore rail wages to 150% above the 1913 level the Department of Agriculture index number for agricultural prices is 24% *below* the 1913 level, and of course the railroad employes as consumers have the benefit of these prices. This illustrates vividly Secretary Wallace's argument for restoration of the pre-war "parity" between what the farmer produces and what he must buy. Freight charges enter into all prices and into many important products they enter several times. An important producer of pig iron has calculated that 63% of the cost of it at the furnace is for transportation of the materials. When pig iron or steel

is transported to a manufacturer of agricultural implements another charge is incurred, and when the implements are redistributed, one or more additional charges are incurred, all of which must enter into the price of the implements, and so of other goods.

Obviously neither the railroad companies nor the shippers or consumers of the goods which comprise the bulk of rail traffic are now in position to pay higher rail wages and from what other source are they to be paid? This rail case illustrates very clearly the fallacy of the theory that aggregate purchasing power can be increased by increasing costs which must be added to the prices of the goods or services produced. Moreover, it illustrates the general state of disorder in economic relations which has been the cause of the depression and now protracts it.

Why Unemployment and Low Prices Persist

Every group in the economic system pays for what it buys from the other members of the system, with its own products and services. The system virtually is an organization for exchanging services, and prosperity depends upon such balanced relations in production and trade as will enable the markets to clear themselves without troublesome surpluses and all of the products to enter consumption. All of the disorders of the system, such as overproduction, underconsumption, abnormally low prices and wages, unemployment, etc., result from unbalanced relations.

The railroad employes stress the fact that 40% or more of their number are out of employment, which of course is a distressing condition, but a glance at the chart and table affords an ample explanation. The change in relations between transportation costs and the values of the primary products which comprise the bulk of the traffic has been one of the principal causes of the decline in trade which in turn has resulted in the state of unemployment on the railroads and in the industries. And whatever devices may be tried, it is safe to say that the situation will not be remedied until the people are able to buy each other's products with their own.

One of the arguments for inflation of the currency has been that it would relieve the groups whose compensation is now depressed, and all debtors, by restoring normal relations throughout the system. One of the plausible representations has been that inflation would accomplish an unobserved reduction of wages along with the reduction of indebtedness, but the American Federation of Labor has given notice that it will demand wage increases to compensate for any reduction in the purchasing power of the money. This is a perfectly logical claim when the policy is necessary to maintain balanced relations, but if carried out under present conditions will defeat the efforts of Secretary Wallace to correct the maladjustments which have prostrated agriculture and been the most obvious cause of the depression.

This subject was discussed in the August number, 1932, of this publication—twenty-one months ago—and we can do no better than reproduce a part of what was said then:

> Nobody has intended to deadlock industry. The great advance of wages followed rather than led a similar advance of farm products, and so long as the general price level was maintained the flow of trade and the activities of industry were uninterrupted, but when goods and services could no longer be exchanged on a common basis the deadly depression set in. It may be said that the wage-earners in the factories and on the railroads are not responsible for the fall of farm products, but it is not a question of responsibility. The effects of the unbalanced relations are as disastrous in the factories and on the railroads as on the farms. Prosperity is not in mere wages or in mere prices, but in the mutual relations throughout industry.
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> If it were practicable for the millions of unemployed to barter the services which they have been accustomed to render direct for wheat, butter, eggs, meat, milk, cotton, wool, etc., no doubt they would be willing to do it upon terms not very different from those upon which the exchanges have been made in the past, but under the complex organization of modern industry this is impossible, and when the exchanges are made through the medium of money, at the present scale of prices, the farmers' buying power is reduced to only one-half or less of what it formerly was.
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> We repeat that the wage-earners in the factories, upon the railroads and elsewhere have not consciously sought to gain an advantage over the farmers. Apparently they believe that in opposing wage-reductions they are only trying to hold their own, and that their wage-rates have no relation to the farmer's compensation. This is a mistake, for the purchasing power of a fixed wage increases as the cost of living declines, and increases at the expense of the producer whose products or services are declining. This increase means that the wage-earners (in so far as they are able to hold full-time employment) are able to command an increasing share of all production, while the 42 per cent of the population which is classed by the census as "rural" has at its command a decreasing share of all production.
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> This is unfair, and not only unfair but unworkable, for the economic law does not permit it. If the wage-earners could pick their gains out of the sky they might enjoy them, but when they come out of other sections of the population the loss of purchasing power by the latter inevitably forces wage-earners out of employment, as witnessed in the last two years. It has upset the "sound, fair balance" in the industrial system. The whole situation affords another demonstration that the basis of sound economics is the moral law. In truth, the economic law and the moral law are one and the same.

In Conclusion

We have dealt thus at length with the question of the balance in the economic system because the events of the month have importantly affected that balance, and have invited the comments; and also because in the general situation there have been developments holding high promise of recovery if they receive the support of sound trade policies.

The uncertainties created by the pressure of new inflationary proposals in Congress have been substantially allayed by President Roosevelt's firm stand against the chief of

these measures, the Dies-Thomas silver bill; and by the refusal of the House to consider other measures which had been actively supported. Moreover, the assurance of the Treasury that gold will be forthcoming for export whenever the dollar goes below the "gold point" in relation to other gold currencies is the most specific contradiction that could be given of the various rumors that further devaluation of the dollar is presently intended.

Doubtless in some quarters there is a feeling of disappointment that the current inflationary proposals are not making more headway, based upon the familiar argument that while the price advance has not come up to expectations thus far, it would surely do so if another dose or two of inflation were given. But excess banking reserves are already sufficient to support an addition of fifteen billions of dollars to the existing volume of bank credit; and the President holds permissive powers, under the Thomas amendment, to enlarge the reserves by huge additional sums. This being the situation, he recognizes that further measures to create money or credit constitute nothing but danger. Bank credit is as truly money as the currency which is employed as the small change of business; and if the money is available and is not being called into use, the next step is to inspire the confidence and establish the business conditions that will put it to work, rather than to devise ingenious schemes for adding to the supply.

Investors are heartened by every indication of intention to maintain the value of the dollar. The reports that amendment of the Securities Act for the purpose of facilitating new security issues is under consideration are equally encouraging. Both policies are necessary to lay a basis for revival of the capital markets and for improvement in the capital goods industries, which are now the chief areas of depression.

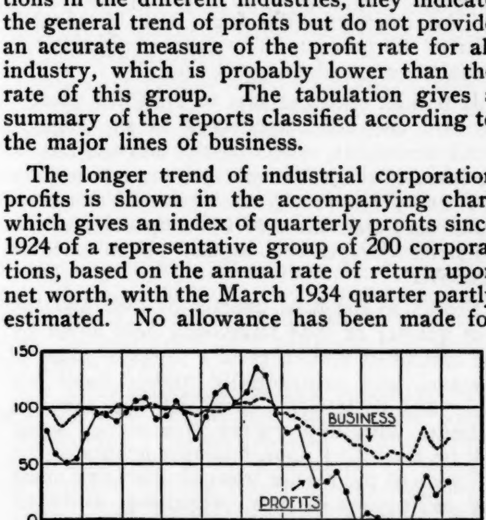
Furthermore, the fact that Government expenditures are running below estimates is reassuring. The new regulations for more economical administration of relief work reveal the intention to confine this class of expenditures to the relief of distress, rather than to employ them as an agency to stimulate business. This tends to uphold confidence in the Government finances.

These gains have created a better business feeling, and they emphasize the importance of shaping all policies and efforts to reestablish equitable relations within the economic system. The psychological improvement will carry trade forward, revive the demand for capital goods, and put the unused bank credit to work, if the conditions essential to the free exchange of goods are restored; and these conditions are simply that the terms of exchange shall be fair and just, and on such levels as will clear the markets and give people work. What is now needed is acceptance of this basic economic principle, and the intelligent cooperation of all elements of the community in applying it.

First Quarter Profits

Earnings reports published during the past month by a group of 210 industrial companies show for the first quarter of 1934 a combined balance of net profits over deficits of $98,000,000, which compares with a profit of $72,000,000 in the preceding quarter and a deficit of $23,000,000 in the first quarter of 1933. Among individual companies the majority of the changes were in the direction of improvement, either through increased profits or a decrease in the size of deficits. In relation to invested capital the level of corporate profits is still relatively low, although of course the results are much better than those of the first quarter a year ago, which period marked the lowest point reached in business activity, the lowest point in prices and the closing of all the banks. This year approximately 71 per cent of the companies thus far reporting were operating in the black, as compared with 63 per cent in the preceding quarter and only 40 per cent in the first quarter of 1933. As these figures are based only on the companies which issue quarterly statements, and therefore include many of the largest and most successful organizations in the different industries, they indicate the general trend of profits but do not provide an accurate measure of the profit rate for all industry, which is probably lower than the rate of this group. The tabulation gives a summary of the reports classified according to the major lines of business.

The longer trend of industrial corporation profits is shown in the accompanying chart which gives an index of quarterly profits since 1924 of a representative group of 200 corporations, based on the annual rate of return upon net worth, with the March 1934 quarter partly estimated. No allowance has been made for



Quarterly Index of Industrial Corporation Profits and the Annalist Index of Business Activity, 1926=100

FIRST QUARTER INDUSTRIAL CORPORATION PROFITS

Net Profits Are Shown After Depreciation, Interest, Taxes, and Other Charges and Reserves, but Before Dividends.

Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.

(In Thousands of Dollars)

No.	Industry	Net Profits First Quarter 1933	Net Profits First Quarter 1934	Per Cent Change	Net Worth January 1 1933	Net Worth January 1 1934	Per Cent Change	Annual Rate of Return % 1933	Annual Rate of Return % 1934
1	Autos—General Motors....	$ 6,870	$29,411*	+328.1	$ 860,869	$ 871,498	+ 1.2	3.2	13.5
9	Autos—Other	D-5,082	D-3,742	....	192,226	179,243	— 6.8	......	......
13	Auto Accessories	D-2,180	2,323	+	93,947	88,565	— 5.7	......	10.5
6	Baking	4,304	4,287	— 0.4	263,485	255,133	— 3.2	6.5	6.7
7	Building Materials..........	D-2,932	D-850	....	143,259	139,177	— 2.8	......	......
14	Chemicals	9,789	22,528	+130.1	914,642	925,490	+ 1.2	4.3	9.7
5	Coal Mining..........	D-287	1,307	+	77,877	76,718	— 1.5	......	6.8
7	Drugs and Sundries..........	1,819	2,152	+ 18.3	39,780	37,236	— 6.4	18.3	23.1
7	Electrical Equipment......	D-2,566	1,799	+	621,716	590,872	— 5.0	......	1.2
15	Food Products—Misc.......	13,770	20,660	+ 50.0	519,457	536,287	+ 3.2	10.6	15.4
7	Household Supplies..........	1,718	5,010	+191.6	162,553	163,667	+ 0.7	4.2	12.2
1	Iron & Steel—U. S. Steel	D-16,730	D-6,990	....	1,911,145	1,869,187	— 2.2	......	......
17	Iron and Steel—Other......	D-17,574	D-1,343	....	1,427,281	1,372,600	— 3.8	......	......
9	Machinery	D-1,372	1,701	+	93,549	91,824	— 1.8	......	7.4
5	Merchandising	D-2,222	25	+	84,516	85,713	+ 1.4	......	......
8	Mining, Non-ferrous........	D-730	1,196	+	162,450	154,450	— 4.9	......	3.1
5	Office Equipment..........	924	3,072	+232.5	127,666	113,835	—10.8	2.9	10.8
15	Petroleum	D-11,916	5,865	+	758,212	759,415	+ 0.2	......	3.1
5	Restaurant Chains..........	D-263	37	+	52,784	48,310	— 8.5	......	......
7	Textiles & Apparel..........	D-49	1,274	+	72,323	60,691	—16.1	......	8.4
35	Misc. Manufacturing........	2,007	6,798	+238.7	516,637	491,509	— 4.9	1.5	5.5
12	Misc. Services..........	28	1,308	+	248,107	227,595	— 8.3	......	2.3
210	Total	D-$22,674	$97,828	+	$9,344,481	$9,139,015	— 2.2	......	4.3

D- Deficit. * Preliminary.

seasonal variation, for the reason that the abnormal conditions of recent years have caused such wide fluctuations, although the apparent tendency in this group is for the second quarter to contribute somewhat more than an average share of the year's earnings, followed by the third and the first, with the fourth quarter the poorest. The chart gives also the Annalist index of business activity.

It will be observed that in the third quarter of 1933 the index recovered to the highest point since 1931, reflecting the unusual rise in business activity that reached its peak in July and was prompted by the desire of manufacturers and merchants to build up depleted inventories before the higher prices became effective.

Profits in the final quarter of 1933 and the first quarter of 1934 have been held down by the combined influences of a lower volume of business and substantially higher costs for labor and materials. It is still too early to estimate with any degree of accuracy what will be the effect upon business profits in the full year of the higher level of operating costs and selling prices now prevailing, although there is no doubt but that the higher level of costs has made it increasingly difficult for representative companies to show reasonable profits and for the large numbers of borderline concerns to break even.

Money and Banking

The volume of surplus bank reserves continued to increase during April, and on the 18th stood at a record "high" in excess of $1,600,000,000. While part of this increase was caused by the import of $34,000,000 of gold between the 1st and the 18th, a more important factor was the action of the Treasury in utilizing a part of its gold stocks in making disbursements. What happened was that the Treasury deposited gold certificates (issued against its gold holdings) with the Reserve Banks, and drew on the resulting balances, instead of calling in its deposits with commercial banks. The effect was to put added funds in the market and swell member bank reserves. During the four weeks ended April 18, the volume of gold certificates so deposited exceeded the rise in monetary gold stocks by about $100,000,000, indicating the extent to which existing gold stocks were being drawn into use. It is understood that gold so used does not represent any of the "profit" on revaluation, but is part of a supply of "free" gold, over and above the revaluation "profit" and not held in any specific currency reserve.

Money rates were generally unchanged, except that bill rates, under the pressure of idle funds, dropped to new low levels, 90-day maturities going to ¼ bid, 3/16 asked. Yields on

weekly offerings of Treasury bills continued around 0.08 per cent for 90 days and 0.18 per cent for 180 days.

Bank deposits increased steadily during the month, but volume of loans and investments remained practically unchanged. Since January, loans and investments of the weekly reporting member banks have advanced approximately $1,000,000,000, but the advance is almost wholly accounted for by increased purchases of Government securities incident to the Government's large borrowing program. The total of loans and advances has not yet increased; in fact, "all other" loans alone, which include commercial loans along with other loans not specifically covered by security collateral, were lower in April than in previous months.

Dollar Touches Gold Export Point

An interesting development of the month was the drop in the dollar to a point where gold shipments to France and Holland would have been profitable, thus affording the first test of the willingness of the Government to permit gold exports in defense of the recently established new gold parity. This weakness accompanied strong pressure in Congress for mandatory silver legislation and rumors abroad of a pending further devaluation of the dollar. With the approach of the dollar to the gold point, there was a good deal of speculation as to whether export licenses would be granted. As soon as the market became assured on this point, and as the President made known his opposition to radical inflationary measures, confidence in the dollar revived, and there was a quick rebound in the rate before any actual shipments were arranged.

With the restoration of confidence in the currency, Government bonds turned strong, most of the longer issues advancing to new high prices, while Treasury 3s of '51-55 reached par for the first time since their issuance in September, 1931.

United States Government Finance

In April the Government carried through another major conversion operation in effecting an exchange of approximately $1,000,000,000 of new 3¼ per cent bonds due in 1946 for $815,000,000 of Liberty 4¼ per cent bonds called for payment April 15 and $234,000,000 of Treasury notes due May 2. The operation constituted a second step in the refunding of the Fourth Liberty Loan, the first having been taken last October, when the Treasury announced its intention of calling $1,900,000,000 of these bonds for payment in April, and at the same time offered holders the option of immediately converting both called and uncalled Fourth Libertys into new 10-12 year bonds bearing interest at 4¼ per cent for one year and 3¼ per cent thereafter. It will be remembered that $900,000,000 of the called bonds were converted at that time, leaving $1,000,000,000 to be dealt with at the call date in April. Of this total, $815,000,000 has now been tendered in exchange for new 12-year 3¼s. Inasmuch as cash redemptions are understood to have been light, it is assumed that the balance of securities unconverted reflects the usual tendency of many small investors to overlook maturity dates.

The foregoing figures, together with the rise of the new bonds to more than a point premium, have indicated a highly gratifying public response to the Treasury's program. With the completion of this financing the Treasury effects a saving of one per cent interest on the called bonds, while at the same time reducing the amount of the Fourth Liberty loan to be refinanced before maturity in 1938 to $4,367,000,000 against $6,268,000,000 last Autumn. In accordance with its program of anticipating the 1938 maturity, the Treasury has called an additional block of $1,200,000,000 of these bonds for payment in October.

Factors Aiding Treasury Finance

In carrying forward these refunding operations, the Treasury has been aided by the enormous supplies of funds, which are reflected in excess reserves of the banks amounting to over $1,600,000,000. Under pressure of this huge volume of idle money, yields on short-term Government securities dropped as low as 0.07 to 1¾ per cent for maturities ranging from three months up to three years, and this has tempted investors to an increasing extent into the longer issues.

Besides the easy money factor, the Government bond market undoubtedly has been helped by improved sentiment resulting from the fact that the indicated deficit will be much less than forecast in the President's budget message. Whereas a deficit of $7,797,000,000 had been forecast for the fiscal year ending June 30, the actual receipts and expenditures through April 26 indicate that the deficit for the full year will be in the neighborhood of $4,500,000,000, including $488,000,000 expenditures for statutory debt retirement through the sinking fund.

The principal factor in this reduction has been the drop in the net expenditures over receipts of the Reconstruction Finance Corporation and the delay in spending the funds appropriated for the Public Works Administration. The budget provided $3,970,000,000 for the R. F. C., but the balance of expenditures over repayments through April 26 amounted to only $1,336,000,000. One important reason for this is that the purchase of preferred stocks of banks, while amounting to

$577,000,000 by March 31, has fallen far short of the budgeted total of $1,350,000,000. In general, however, the demand for loans has fallen off with the improvement in business conditions, and repayments have increased. Out of total advances of $4,991,000,000, the repayments up to March 31 were $1,292,000,000, or 26 per cent. These repayments have been used as a revolving fund for making new loans, and the collection of interest and dividends has been an added source of income available for relending without recourse to the Treasury. The following table indicates total advances made to private financial organizations and railroads alone and the repayments up to March 31, 1934:

Reconstruction Finance Corporation Loans Under Section 5
(Period of Feb. 2, 1932 to March 31, 1934)

(In Millions of Dollars)

	Total Disbursed	Outstanding Mar. 31, 1934	Total Repaid*	Per Cent Repaid*
Banks & Trust Companies	1,533	657	876	57
Railroads	402	345	57	14
Mortgage Loan Companies	222	162	60	27
Federal Land Banks	194	194	......	....
Regional Credit Companies	170	25	145	85
Building & Loan Associations	114	58	58	50
Insurance Companies	89	51	38	43
Joint Stock Land Banks	15	12	3	20
Livestock Credit Companies	13	2	11	95
Other Loans	21	6	15	71
Total	2,773	1,510	1,263	45

*Exclusive of interest paid and accrued.

It will be observed that the repayments by banks, the largest class of borrowers, have amounted to 57 per cent, reflecting the improvement in the condition of bank assets, the decline of currency hoarding and the increase of bank deposits. This is hardly a true indication, however, of the speed with which the total assets of the R. F. C. can be liquidated, inasmuch as numerous items appearing on its balance sheet cover the purchase of preferred stocks, investment in capital stock of various government subsidiaries and outright grants for relief purposes.

Deficit Still Larger Than Last Year

Notwithstanding that the deficit will be less than expected, it is in order to point out that the indicated total of $4,500,000,000 will be $1,400,000,000 larger than last year, and the largest on record for any peace-time year. Moreover, the statement has been made that such estimated expenditures as were not made in 1934 would carry over into the following year, so that while the showing for 1934 may prove more favorable than anticipated that for 1935 may prove less so, unless, of course, there should be a further substantial improvement in business conditions. The cumulative deficits since December 31, 1930 have increased the public debt from $16,026,000,000 to $26,121,000,000 at the present time, and if the expenditure program is carried through as originally planned the total debt will reach $31,834,000,000 by June 30, 1935.

Taxes and National Income

An inevitable accompaniment of the increased expenditures of the Government has been the mounting burden of taxation which has absorbed an increasing share of the national income. According to figures recently published by the National Industrial Conference Board, the total of all taxes collected in the United States—Federal, State and local—in 1929 amounted to $9,800,000,000, or approximately 11.8 per cent of the national income then estimated at $83,000,000,000. By 1932, taxes, despite the higher rates in effect, had fallen off to $8,000,000,000, but as the national income had fallen even more rapidly to $39,400,000,000, the percentage of income taken as taxes rose in that year to 20.3.

With 20 cents out of every dollar of income taken by the Government and its sub-divisions, the burden that is being placed on private enterprise is becoming a constantly more serious matter. Moreover, these burdens are still increasing, not only in connection with Federal expenditures, but also in connection with the local governments which do not command the same facilities for placing their loans as does the Federal Government, and which are therefore forced to resort to higher tax rates in order to maintain their budgets in the face of tax delinquencies and added demands for unemployment relief. Unless we can get trade back on a self-sustaining basis and achieve a rise in the national income, there will be grave danger that the burden thrust upon those still able to pay taxes will be more than they can bear and cause a further stifling of enterprise.

The New Revenue Bill

An official estimate of the additional revenues to be provided is $417,000,000, after deductions aggregating $22,000,000 for tax relief upon candy, jewelry, furs, soft drinks, produce futures and bank checks. The most important change in the present law is that affecting corporation returns, which withdraws the privilege heretofore granted to corporations under practically a common ownership of making a consolidated return, subject to an additional tax of ¾%. Hereafter all corporations will have to report separately, each subject to the 13¾% on its own earnings. Dividend income will remain free of tax, but the losses by one or more members of a group will not cancel corresponding profits made by other members. The net gain in revenue by this change is estimated at $35,000,000, but it may be doubted that any accurate calculation can be made in advance. Certainly the act will promote actual consolidations where that

is practicable and savings can be effected. However, in cases where corporations are located in different states differing corporation and tax laws may be an important consideration. Again if the corporations are interdependent, as in case of one producing supplies or parts for others, the question of profits or losses in their dealings with each other may raise complications. Obviously their relations cannot be as exclusively intimate and private as if they were not a matter of public concern. Perhaps the most serious effect to be apprehended is the disturbance it may cause in the affairs of some of the largest business organizations in the country. It cannot be regarded as a constructive influence at this time, when there are so many uncertainties to take account of.

The tax of $1 per $1,000 on the "declared value" of capital stock, which was in force for some years and repealed in 1926, then restored in the Recovery Act to expire June 30, 1934, is reenacted. This applies to net worth, i.e., net value of capital, surplus and undivided profits, less indebtedness, and there is an excess profits tax of 5% upon any net income over 12½% of capital. Changes in the computations of capital gains and losses of individuals are planned to effect a further elimination of offsets, and increases in the medium brackets of the super taxes are expected to increase these returns by $25,000,000. The estate tax is increased, the rates running up to 60% on that portion of estates over $10,000,000.

In view of the heavy deficit in the budget it must be agreed that there is a strong prima facie case for increasing the revenues, but it should not be supposed that this taxation will increase the aggregate purchasing power of the nation. Every dollar of it will reduce the purchasing power of the taxpayers in equal amount, and in view of the admitted need for capital expenditures upon the industries it may be asked whether more would not be accomplished for the stimulation of private enterprise by allowing the industries to keep these sums for their own uses than by diverting them by taxation into the various governmental channels of expenditure. It is a subject of comment that the capital goods industries are lagging in activity, either because the industries are without funds of their own for improvements or replacements or because they are unable to borrow for the purpose. Perhaps if they were able to accumulate a backlog of their own, or had a more hopeful prospect of making profits, they might be able to manage the financing themselves and have a stronger inclination to do so. With so important a line of industry as steel showing losses for the first quarter of 1934 it would seem that consideration for future revenues as well as for a revival of the capital goods industry might raise a question as to the wisdom of further additions to taxation.

A Study of Corporation Profits, 1919-1932

Last month we gave an extended review of Bulletin 49, recently issued by the National Bureau of Economic Research, Inc., devoted to a study of the aggregate income of the people of the United States in the four years 1929-1932. The Bulletin was an advance summary of an expert study made by this Research Bureau, under the auspices of the Department of Commerce, in response to a resolution of the United States Senate.

Inasmuch as the complete report (*) contains 260 pages, with over 200 tables and 16 charts, the Bulletin quoted from could give only the more important features and our review could touch upon only a portion of these, but the latter gave the ultimate figures for income distribution by principal groups of industries and employment. Our discussion concluded with the statement that there was much more to be said about the distribution of the national income and that we would return to the subject.

During the past month the National Bureau of Economic Research has issued Bulletin 50 in the series of economic studies to which a footnote reference was made in our April issue. It is entitled "Recent Corporate Profits in the United States," and was prepared by Mr. Solomon Fabricant, who has been associated with Professor Frederick C. Mills, of Columbia University, in the preparation of a number of the Bureau's publications treating of production and profits. (†)

Bulletin 49 analyzed and discussed the individual incomes of the people of the United States as computed from Government statistics, and Bulletin 50 deals with the incomes of corporations. Thus the two inquiries are related to the same general subject, but in their details they do not cover the same ground. As stated in our article last month, the ultimate object of all industry and business is to supply the wants of the population, and in the last analysis everybody's real income is received in the form of goods and services. Therefore, statisticians begin at production and trace the goods and services

* This publication known as Senate Document 124, Seventy-third Congress, is now on sale by the Superintendent of Documents, Washington, D. C. Price, 20 cents.

† For the information of our readers we gave last month a brief footnote statement regarding the National Bureau of Economic Research, Inc., explaining that it is a no-profit organization for impartial research upon economic subjects, giving a list of its officers and describing the methods by which its Board of Directors is elected.

produced through all transfers to their disappearance in the hands of the ultimate consumers. They seek to answer the two questions: what was the money value of the aggregate product, and how was the product divided at the point of consumption?

Excepting agriculture and perhaps construction, production in the United States is mainly carried on by corporations. Bulletin 49 gave the aggregate value of goods and services entering into trade, and the aggregate of money incomes received as wages, salaries, dividends, interest payments, rent, royalties, proprietors' profits, etc. Bulletin 50 is confined to an examination of the net earnings of corporations. All of the data are from the income tax reports of the United States Bureau of Internal Revenue, to which all corporations are required to make returns, duly attested by the responsible officers, who are personally subject to criminal prosecution for false reports, and the returns are subject to the scrutiny of experienced accountants, familiar with every scheme of evasion. False statements are punishable not only as attempts to defraud the United States Government, but for perjury.

Complete returns in the aggregate are not available to the public until two years after the year to which they refer and when these figures were compiled the returns for 1931 were the latest fully available, although preliminary estimates for 1932 are given.

The report includes all corporations except those largely tax-exempt, "such as cooperative, charitable, educational and labor organizations, Federal Land Banks, and life insurance companies." Excepting these, the figures represent corporate earnings in all kinds of business.

The Bulletin makes the following preliminary statement:

The data compiled by the Bureau of Internal Revenue not only provide the facts as to profits; they also give a composite picture of operations not generally made available even by the large corporations that publish financial statements. The details regarding receipts and deductions, included in the aggregate income account of all corporations, help to throw light upon the methods underlying the computations of profits. The nature of the accounting estimates of profit, and the approximate character of the reported figures on corporate earnings, may be made clearer by a study of these materials. The present Bulletin is based upon these comprehensive Federal data.

We have space in this issue for only the principal table, No. 3, which gives the ratio of net profits to net worth, with the corporations classified in eight groups. It will be seen that in 1931 and 1932 their operations resulted in a net deficit on the consolidated returns, the losses of those having deficits exceeding the gains of those having profits. This was true also in 1921, another of the fourteen years which some of the tables include. Table 3 gives the analysis by groups in only six years:

Table 3—Rate of Return On Book Value of Stock Equity, 1927-1932

All Corporations in the United States

(Excluding tax-exempt corporations and life insurance companies)

	Ratio of Net Profits after Tax to Book Value of Stock Equity,† in Percentage Form						Ratio of Net Profits after Tax, plus Compensation of Officers,‡ to Book Value of Stock Equity,† in Percentage Form			
Industrial group	1927	1928	1929	1930	1931	1932*	1928	1929	1930	1931
Agriculture and related industries	1.3	2.2	1.4	—2.8	—5.2	—5.9	3.7	3.1	—1.1	—3.9
Mining and quarrying§	0.7	1.8	2.7	—0.0	—2.7	—2.2	2.5	3.2	0.6	—2.1
Manufacturing	6.2	7.6	8.3	2.6	—1.0	—2.5	9.7	10.5	4.7	0.8
Construction	9.9	7.4	7.4	5.4	—1.0	—7.3	19.1	18.5	15.6	8.6
Public utilities and transportation	4.8	5.1	5.8	3.6	2.0	0.6	5.4	6.1	3.8	2.2
Trade	5.5	6.4	4.9	—0.5	—4.5	—6.7	12.8	11.7	6.1	1.8
Service	4.0	4.1	3.8	1.8	—2.3	—10.8	10.2	8.2	6.3	2.5
Finance and real estate	5.6	6.4	5.3	1.6	—1.8	—2.8	8.3	6.8	3.0	—0.4
Grand total¶	5.3	6.2	6.2	2.2	—0.8	—2.3	8.2	8.1	4.0	0.9
Manufacturing subgroup										
Foods, beverages and tobacco	6.7	7.9	7.7	6.3	3.9	2.0	9.8	9.5	8.3	5.8
Textiles and products	5.4	3.5	2.9	—5.8	—6.4	—7.2	7.2	6.9	—1.7	—2.4
Leather products	7.4	4.8	3.9	—3.2	—4.9	—8.0	8.6	7.8	0.7	—1.1
Rubber products	5.1	0.3	2.5	—4.4	—2.4	—5.9	1.5	3.7	—3.4	—1.3
Lumber products	1.0	2.4	2.4	—4.5	—8.3	—9.8	5.2	5.2	—1.9	—5.9
Paper, pulp and products	6.7	7.1	6.4	2.9	—0.5	—3.8	9.5	8.5	4.9	1.3
Printing and publishing	9.7	11.9	11.5	7.6	2.2	—1.0	18.3	18.0	13.6	7.4
Chemicals and allied products	5.4	9.1	9.9	5.0	1.1	1.2	10.0	10.7	5.8	1.7
Stone, clay and glass products	6.2	6.5	6.2	1.8	—2.0	—5.1	8.8	8.7	3.9	0.1
Metal and its products	7.1	8.8	10.9	3.3	—2.1	—3.9	10.5	12.7	4.9	—0.6
Manufacturing not elsewhere classified	6.1	7.5	5.7	—0.7	—4.4	—6.3	11.6	9.5	3.0	—0.5
Total manufacturing	6.2	7.6	8.3	2.6	—1.0	—2.5	9.7	10.5	4.7	0.8

* Preliminary estimates.

† The balance-sheet figures published in "Statistics of Income" have, on the basis of estimates, been raised to include corresponding items of corporations not making balance-sheet reports. Book values are as of the end of the year, except for 1932, for which 1931 values have been used.

‡ Data for 1927 and 1932 are not available.

§ See text, footnote 7.

¶ Includes a small group of corporations not reporting the nature of their business.

The Salary Question

On account of present interest in compensation of officers, and a question as to the extent to which such payments may have been made a means of distributing profits to escape the corporation income tax, two computations of the rate of net earnings are given, one showing the percentage of net earnings after tax to book value of stock equity, and the other the percentage of net earnings plus compensation of officers to the book value of the stock equity. In other words, the second calculation shows what the net earnings percentage would have been if the officers had given their services for nothing. Concerning this calculation the author says:

> Of course, in all these industries payments to officers represent only in part distributions of profits. To a large extent they are actual costs. But because in many corporations they are made at least partially in lieu of dividends, it is necessary to consider them in comparing the rate of return of one industry with that of another.

We are lacking space in this number to discuss this phase of the subject beyond remarking that Bulletin 50 itself carries evidence that salaries are a notably smaller factor in the net earnings of the corporations of above $1,000,000 net assets than in those whose assets are under that figure.

The Showing of Corporate Profits in Table 3

Table 3 does not begin as far back as Table 1, but reveals that not only did all corporations in the aggregate pay out more than they received in 1931 and 1932, but that five of the eleven groups also had deficits in 1930. Moreover, it may be noted that Printing and Publishing, Chemicals and Allied Industries, with Foods, Beverages and Tobacco led all the other branches of manufactures and raised the average of the totals. All of these, but particularly the first named, were helped by the boom period, and the last named suffered the least of any in the reaction. Chemicals were a comparatively new industry, a fact always favorable to profits.

Table 3 shows not only the average rate of net earnings for each of the classified groups in each of the six years reviewed but the average of each group over the six years, and the average of all groups in each year; also a similar statement for each of eleven manufacturing sub-groups. It will be seen that the highest average profit for all the corporations in any year was 6.2%. For all the manufacturing groups the highest average for any year was 8.3%, and over the six years 3.5%.

These calculations are based upon the book value of the stock equity; in other words, arrived at by computing the profit after the payment of interest on indebtedness, upon the net worth as shown by the balance sheet, which means net value of the assets after deducting indebtedness.

Attempts frequently are made to discredit such statements of profits by general assertions that book values for capital investment are unreliable, being often inflated by consolidations or by arbitrary revaluations, etc. It will not be denied that a degree of uncertainty attaches to all capital values, particularly where they have been built up over a considerable period of time. It is not denied that in some instances book values and stock issues have been inflated, and it is also true that even where it can be shown that every dollar of the stated capital was invested in cash, there remains a question as to whether the original value may not have been impaired by obsolescence, changes in the line of business, or other developments affecting earning power.

There is good reason for believing that on the average net worth figures are not nearly so far from reproduction costs as critics represent, but because of the degree of uncertainty inevitably attaching to them we have adopted the practice of checking them by profit percentages based upon the aggregate volume of sales or gross income, i.e., the volume of business handled. In the case of sales of products or services of any kind the margin of profit represents the share of the values sold to the public which the corporation was able to retain for its services. It is true that there may be some income from investments outside of the regular business, but except in the case of financial companies, i.e., companies organized for holding stocks and bonds, this is a comparatively small factor. In the case of industrial companies such income usually represents reserve capital. If a part of the capital is employed outside of the regular business, it obviously is not employed in the regular business, and the effect upon the stated rate of profit would depend upon whether the outside earnings would raise or lower the average, and the difference either way would be slight.

Special interest attaches to the profits of corporations engaged in manufacturing, because the division of the proceeds of these industries between capital and labor is a matter of especial concern.

We gave last month (p. 59) a table showing the net taxable income of all manufacturing corporations in the fourteen years 1919-1932, as taken from "Treasury Statistics of Income," in order to show the rate of profit as computed on gross income. We repeat that table herewith, for one reason, because it gives the figures for all of the post-war years and also for the comparison with above figures based on "net worth," which for simplicity we will call capital:

All Manufacturing Corporations in the United States
(In Millions of Dollars)

Calendar Year	Number of Cos.*	Sales or Gross Income	Net Income After Taxes	Per cent Net to Gross
1919	67,852	$ 52,290	$ 3,493	6.68
1920	78,171	56,649	2,337	4.13
1921	79,748	38,442	D-473	D-1.23
1922	82,485	44,683	2,251	5.04
1923	85,199	56,221	3,086	5.49
1924	86,803	53,911	2,334	4.33
1925	88,674	60,830	3,154	5.18
1926	93,244	62,495	3,124	5.00
1927	89,816	63,723	2,580	4.05
1928	91,573	67,273	3,366	5.00
1929	92,230	72,132	3,862	5.35
1930	91,504	58,650	801	1.37
1931	89,085	44,033	D-988	D-2.24
1932†	82,733	23,846	D-1,533	D-6.43
14 Year Average	85,651	$53,941	$2,028	3.76

D- Deficit. † Preliminary. * Excluding inactive corporations.

Below are given both computations for the six years covered by Table 3:

Profit Percentage	1927	1928	1929	1930	1931	1932	Av.
On capital	6.02	7.6	8.3	2.6	D-1.0	D-2.5	3.5
On gross income	4.05	5.00	5.35	1.37	D-2.24	D-6.43	1.18

D-Deficit.

The total of profits, of course, was the same in both calculations, the changes in capital were comparatively small, and the declining rates of profit resulted mainly from falling prices and the declining volume of turnover. In years when the volume exceeded the capital the rate of profit computed on sales obviously would be lower than the rate on capital, and in the later years when volume of sales was less than total capital the percentage of profit on sales was larger than on capital until the profit disappeared, after which the percentage of loss continued to increase over the percentage based on capital. The volume of business turned over by the corporations in 1927 was $63,723,000,000 and in 1932 $23,846,000,000. Aggregate capital or "net worth" in 1927 was $48,050,000,000 and in 1932 $47,740,000,000. The two calculations serve as a check on each other, and in either one the rate of profit is lower than is commonly expected in ordinary merchandising, which has no such risk in fixed investments as manufacturing.

The Total Share of Capital

In order to arrive at the total share of all capital in the values created or handled by these corporations it would be necessary to add to the profits here shown the interest charges paid by them for the use of capital borrowed or property rented outside of these corporations, i.e., of no profit corporations,—as life insurance companies, benevolent foundations—or individuals; also the profits of outside capital upon raw materials or unfinished goods entering into their products. This information is not available. However, whatever interest, rentals or profits upon other capital were paid by the manufacturing corporations were paid for the use of capital additional to their own, and it is improbable that such returns would average higher than the earnings of the corporations on their own capital. Over the three years preceding the depression, which were better than average years for volume of business, this average was about 5½%. It appears safe to say that upon full analysis the share of all capital employed by corporations in the production and distribution of goods and services of every kind during the fourteen-year period 1919-1932 would be found not to exceed 5% of the total values produced or realized by the said corporations.

In Conclusion

This is the most complete calculation of the profits of the business corporations of this country that ever has been made, and the authority for it is unimpeachable. The result is literally destructive of the representations which have been the ammunition for the main assault upon the economic system under which this country has had its development. It is not too much to say that it furnishes the basis for a defense that will give a complete vindication of the fundamental principles upon which the system is based. Nobody claims that the economic system functions perfectly, for how could it be expected to do so over all the interference with which it has to contend. The economic system is not responsible for war or for inadequate and defective banking laws, or for other impracticable legislation, or other acts of political government which disregard and violate economic law as defined by the masters of that science with practical unanimity. Nor is it responsible for the disagreements within the system which impair its efficiency, in any other sense than that it is a free system, allowing all participants to bargain among themselves over the terms upon which they will cooperate.

For example, the wage controversies which unquestionably present a problem, are incidental to the right of free bargaining between all the economic groups. Obviously all of the groups are necessary to each other, and successful operation of the system is dependent upon voluntary and harmonious cooperation. It is impossible for any important part of the system to coerce any other important part. That would mean civil war, and even if one combination of groups triumphed over the rest it could not compel willing and effectual cooperation. The system depends upon an intelligent understanding of mutual interests.

Refutation of Communist Oratory

This showing of corporation profits is so different from common representations of them that many readers who have had their ideas on the subject shaped by sensational press reports and the speeches of agitators may hesitate to accept them. That will not be the case with persons who have taken the trouble to inform themselves from trustworthy sources. It completely discredits statements to the effect that 2 or 3 or 4% of the population enjoy 75 to 90%, or some such proportion, of the national income. Indeed, there was not much left of that when Bulletin 49, discussed last month, showed that in 1929 wages and salaries alone equalled 65.2% of the total income distributed and in 1932 64.5%, with the farmers, professional classes and small traders and operators yet to be accounted for. Not only were the money incomes from the industries widely distributed, but it is common knowledge that the products and services of the industries were broadly distributed. To only a slight extent are the vast industries of this country employed in supplying the wants of the rich.

In view of the low margin of corporation profits year after year as shown by the tables it is in order to ask the critics who have insisted that all groups but the farmer have effective control over the prices of their products, to explain how they account for the moderation displayed?

In the light of this showing is it more reasonable to believe that these profits were deliberately contrived and fixed by the recipients or that they have resulted from the uncontrollable operations of economic law? And if the latter is true, what becomes of nine-tenths or more of the indictment against the free economic system?

The Social Use of Private Wealth

Moreover, it is to be considered that of the approximate 5% of the income of corporations which they may be able to retain as their compensation for capital employed and services rendered, a substantial portion is not distributed to stockholders but devoted to the enlargement of the industries; which means increasing the supply of goods and services on the market, and is a social use. Such profits may never be withdrawn, and the properties may become obsolescent and without value. Mr. Ogden Armour once told a Congressional Committee that approximately 78% of all the profits of the Armour industries from their beginning had been left in the business for its development, and it is common knowledge that Mr. Armour at death left an estate comparatively small in proportion to what his fortune at one time had been estimated. If the Armour industries had belonged to a socialist state a similar withholding of earnings from distribution would have been necessary in order to keep the industries up to the growing demands upon them.

The revelation of outstanding importance is that the net earnings of the corporations available for distribution to their stockholders (itself a wide distribution) probably average less than 5% of the sales-value of their products and services. This means that the possibilities involved in the popular demand for "a more equitable division" of current wealth production are necessarily confined to less than 5%. It is impossible to divide any more than all there is, and that is all that the corporations have been getting over an average period of years. The findings also suggest one other reflection, to-wit: Having regard for the fact that all economic activities consist of an exchange of goods and services, how much is the available supply diminished by the widespread misrepresentations of the facts now revealed in Bulletins 49 and 50 of the National Bureau of Economic Research, the reports of the United States Bureau of Internal Revenue and Senate Document No. 124, Seventy-Third Congress?

Further Discussion

We are aware that critics will say that the "averages" shown by these tables conceal wide differences in the profits of corporations, which is the substance of the criticism of the system. We shall give attention to these inequalities in further discussion, but this article occupies all of the space that can be spared to it in this number. We suggest that readers interested in the subject of income distribution preserve the April and May numbers, as the tables may be referred to again and they take up too much space for repetition.

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